No. 22,182

United States Court of Appeals

For the Ninth Circuit

Shelton F. Sackett, and KVAN, Inc., a Washington corporation,

Appellants,

vs.

J. Frank Beaman, and Fidelity and Deposit Company of Maryland, a corporation,

Appellees.

BRIEF FOR APPELLEE J. FRANK BEAMAN

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STATEMENT OF THE CASE

For convenience, appellants Sheldon F. Sackett and KVAN, Inc. are referred to as "Sackett," and "KVAN" respectively. Appellee, J. Frank Beaman, is referred to as "Beaman."

This is a suit commenced on April 20, 1967, by Sackett and KVAN against Beaman and Ernest S. Johnston ("Johnston") for declaratory judgment and injunction (R. 1). The subject matter concerns a written contract (R. 185-186) for the sale of stock (hereinafter referred to as "contract of sale") entered into on or about November 8, 1961 (R. 1, 4), allegedly in-

valid because of a purported violation of the Securities Act of 1933, 15 USC § 77q (herein called the "1933 act"); the Securities Exchange Act of 1934, 15 USC § 78j (herein called the "1934 act"); and applicable rules of the Securities and Exchange Commission (17 CFR part 240). (R. 1, 2, 4, 5, 6). 17 CFR 240.10b-5 is for convenience usually referred to as "Rule 10b-5." All such acts and rules are collectively called the "federal securities acts."

The contract of sale was made in 1961 between Beaman and Johnston as the selling parties, and Sackett and KVAN as the buyers, for 2,500 shares of the capital stock of News Publishing Company, a Virginia corporation. The contract of sale provided that of the sums due thereunder, $1,000 was to be paid upon signing and the balance payable at later dates, the major portion of which was to be evidenced by promissory notes (R. 185). Appellants paid the $1,000 upon execution (R. 35, lines 18-19; R. 28, lines 16-19) and the promissory notes called for under the contract of sale were made and delivered by appellants (R. 25-27).

On December 30, 1961, less than two months after execution of the contract of sale, Sackett, on behalf of himself and purporting to act on behalf of KVAN, gave Beaman an alleged notice of rescission with respect thereto and as to the promissory notes (R. 29, lines 15-19).[1]

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[1]Appellants concede that the discovery of the facts presumably giving rise to a cause of action was made in 1961 (Rep.Tr. 43, lines 4-5).

On January 24, 1962, Beaman commenced action No. 518296 in the Superior Court of the State of California, in and for the City and County of San Francisco, against appellants for recovery under the contract of sale and the promissory notes as to the amounts then due, plus fees, interest and costs (herein called the "first state court action") (R. 80). Sackett and KVAN, on April 3, 1964, filed in the first state court action an amended answer and cross-complaint alleging that the contract of sale was void by reason of (i) want of consideration, (ii) material mistake, and (iii) fraud,[1a] both as defenses and as a basis for the cross-complaint (R. 31-38).

The first state court action resulted in:

(a) Judgment at the trial level rendered May 3, 1965, in favor of Beaman as prayed, and denying recovery on the said cross-complaint (R. 22-23).

(b) Judgment affirmed on March 22, 1967 by the Court of Appeal of the State of California, First Appellate District, Division One, proceeding 1 Civil 23182 (R. 219-236).

(c) The judgment became final on May 22, 1967 (R. 195).

On December 24, 1965, Beaman commenced action No. 562356 in said Superior Court against appellants, for recovery of the sums then due under the contract of sale and promissory notes which had not accrued

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[1a]Appellants in the first state court action also argued that negligent misrepresentation (R. 231) and breach of fiduciary obligation (R. 233) were grounds on which the contract of sale could be voided.

at the time the first state court action was begun (R. 86-88). Said action, No. 562356, is herein for convenience called the "second state court action."

On April 20, 1967, *more than five years after the commencement of the first state court action,* appellants filed in the court below their complaint for declaratory relief and injunction against Beaman and Johnston (R. 1). This complaint was the subject of Beaman's noticed motion to dismiss filed herein on May 9, 1967 (R. 18).

On May 3, 1967, appellants filed in the court below an amended complaint for declaratory relief and injunction against Beaman and Fidelity and Deposit Company of Maryland (R. 4). Beaman, on June 13, 1967, filed a noticed motion to dismiss such amended complaint (R. 142).

On July 17, 1967, appellants filed in the court below a noticed motion for a preliminary injunction restraining Beaman from prosecuting the second state court action (R. 176)[2] which was denied by order of the court on September 5, 1967 (R. 282).

Beaman's two motions to dismiss were heard concurrently on July 25, 1967, Honorable Lloyd H. Burke presiding, and resulted in the Judgment of Dismissal with Prejudice, filed in the court below on August 3,

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[2]Appellants, in the court below, attempted by noticed motion to secure a preliminary injunction restraining Beaman from enforcing the judgment in the first state court action. Such motion was denied on May 22, 1967. Appellants attempted to secure a similar injunction from this Court pending appeal (Proceeding No. 21889) and the motion therefor was also denied in June of 1967. Such actions are reflected in the docket entries (R. 280-281).

1967 (R. 267), entered of record on August 10, 1967 (R. 282).

Subsequent to the hearing on said motions but prior to filing the Judgment of Dismissal, appellants filed in the court below on August 2, 1967, a document entitled "Plaintiffs' Proposed Modifications to Form of Judgment and to Findings of Fact and Conclusions of Law" (R. 238), wherein appellants requested that the findings and judgment submitted by Beaman (R. 263-268) "be modified to permit plaintiffs to file an amended complaint for damages" (R. 238, lines 27-28). The court impliedly denied such request (Rep. Tr. p. 45, line 8 to p. 55).

Appellants' Notice of Appeal was filed in the lower court on September 1, 1967, appealing "from the Judgment of Dismissal with Prejudice signed on August 3, 1967, and entered of record on August 10, 1967." (R. 278)

Beaman stipulates, for the purpose of this appeal, that on August 22, 1967, there was paid to him by Fidelity and Deposit Company of Maryland, the sum of $18,870.22, by reason of its liability as surety on an appeal bond in the first state court action.

QUESTIONS PRESENTED

1. Is Beaman entitled to judgment as a matter of law?

2. May a buyer bring a federal suit for an alleged violation of federal securities acts (a) more than five years after accrual of any claim, and (b) notwithstanding an adverse determination in a state court after a full trial on the merits as to his contentions of fraud, misrepresentation and mistake?

SUMMARY OF ARGUMENT

Even if the lower court's denial of appellants' request to amend is properly before this court, such denial was not an abuse of discretion. Beaman is entitled to judgment as a matter of law in that appellants' claims are time barred and are also blocked by the doctrines of res judicata, collateral estoppel and laches. Any deprivation of a federal remedy occurred because of appellants' own acts and omissions.

ARGUMENT

1. NO GENUINE ISSUE AS TO ANY MATERIAL FACT.

(a) Motion for dismissal shall be treated as one for summary judgment.

Kithcart v. Metropolitan Life Ins. Co. (8th Cir. 1945) 150 F. 2d 997, 1000; cert. denied 326 U.S. 777.

(b) The question presented in any summary judgment matter is:

(i) Whether there is any genuine issue as to any material fact and if not,

(ii) whether movant is entitled to judgment as a matter of law.

Turner v. Lundquist (9th Cir. 1967) 377 F. 2d 44, 46;

U.S. v. Carroll (DC Ark. 1962) 203 F. Supp. 423.

(c) No issue of fact.

No issues of fact are apparent to us (appellants have raised none); therefore, we proceed to the question of whether Beaman is entitled to judgment as a matter of law.

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2. THE APPELLATE COURT IS WITHOUT JURISDICTION TO CONSIDER DENIAL OF APPELLANTS' REQUEST TO AMEND.

Appellants' request to amend was made as part of their proposed modification of findings and judgment filed eight days after the trial court's decision on July 25, 1967, to grant a dismissal of appellants' action. The trial court by implication denied such request, and the Judgment of Dismissal from which appellants have appealed (Notice of Appeal R. 278) contains no such reference to the request for amendment or a denial thereof (Statement of the Case, supra, p. 5). Obviously, the form of judgment was prepared prior to the time any request to amend was made and cannot by reasonable interpretation be said to cover the denial of such request.

Since appellants' Notice of Appeal does not refer to the trial court's denial of their request to amend, this Court is without jurisdiction to consider such denial on the present appeal.

Gunther v. E.I. duPont de Nemours & Company (4th Cir. 1958) 255 F. 2d 710, 717.

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3. **IF THE DENIAL OF APPELLANTS' REQUEST TO AMEND IS PROPERLY BEFORE THE COURT, THERE WAS NO ERROR BY THE COURT BELOW IN MAKING SUCH DETERMINATION.**

Assuming, but not conceding, that the denial of appellants' request to amend is properly before the court,

(a) the matter of amendment is within the sound discretion of the trial court.

Caddy-Imler Creations, Inc. v. Caddy (9th Cir. 1962) 299 F. 2d 78, 84;

Canister Co. v. Leahy (3rd Cir. 1951) 191 F. 2d 255, 257; cert. denied 342 U.S. 893 [A District Court has wide latitude in permitting or rejecting amendments to pleadings.]

(b) the trial court did not abuse its discretion in denying appellants' request to amend.

(i) After a dismissal of his action, a plaintiff should move under Rules 59(e) or 60 (b), Federal Rules of Civil Procedure to reopen, rather than request the court to permit the filing of an amended pleading (the procedure appellants chose to follow).

3 *Moore's Federal Practice* (2d edition) ¶15.10 at p. 959.

(ii) No abuse of discretion where requested amendment simply involves a change in legal theory.

Caddy-Imler Creations, Inc. v. Caddy, supra, holding there was no clear abuse of discretion in trial court's refusal to change entire legal theory of the case after introduction of all evidence was complete.

Stanck v. Trailmobile, Inc. (7th Cir. 1960) 283 F. 2d 827, 828, involving the trial court's denial of an oral motion to amend a complaint to change claim for relief from damages to rescission.

Appellants propose an amendment which purports to set forth a claim for damages (Brief for Appellants, p. 6), rather than declaratory relief. No new facts[3] are alleged other than the allegation that Beaman obtained the sum of $18,870.22 on July 31, 1967[4] pursuant to the judgment in the first state court action (R. 252-253).

Nothing more than a change in legal theory is involved. The issue of *when* appellants' alleged claims for damages accrued is discussed below (infra p. 13).

See:

2 *Witkin California Procedure* §191 at pp. 1168-69.

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[3]As distinguished from conclusions of law and appellants' self-serving statements (R. 252-253).

[4]In fact, such sum was received on August 22, 1967, *after* the requested amendment (Statement of the Case, supra p. 5). Appellants were aware of their error at the time of the hearing on the requested amendment (Rep. Tr. 50).

(iii) Leave to amend need not be granted with respect to amendments which would serve no purpose.

The lower court should consider any objections that would defeat the proposed amended claim as a matter of law; otherwise, no purpose would be served by permitting the amendment.

Walker v. Bank of America NT&SA (9th Cir. 1958) 268 F. 2d 16, 26, cert. denied 361 U.S. 903 [Consideration of objection based on statute of limitations in denial of motion to amend.]

Holmes v. Henderson (9th Cir. 1957) 249 F. 2d 529, 530.

Amendment is not a matter of right as suggested by appellants (Brief for Appellants, p. 6). *Cohen v. Gensbro Hotel Co.* (9th Cir. 1958) 259 F. 2d 78, cited by appellants, held that *under the circumstances of that case,* the granting of a *motion to dismiss* was arbitrary and clearly erroneous (at p. 83). In that case, the appellate court simply determined that the defense of equitable estoppel may have been applicable to the facts at hand and defendants were not entitled to judgment as a matter of law.

There are ample grounds on which it can be said that Beaman was entitled to judgment as a matter of law, both as to the two complaints on file (R. 1-7) and the proposed second amended complaint (R. 251-254). See discussion infra.

4. APPELLANTS' CLAIM WAS BARRED BY THE STATUTE OF LIMITATIONS.

(a) The three-year California statute of limitations is applicable.

No federal statute covers any time limitation on the commencement of private actions under the applicable sections of the 1933 Act, the 1934 Act and/or Rule 10b-5. In such cases, the federal courts adopt and apply the local state law of limitations.

> *Holmburg v. Ambrecht* (1946) 327 U.S. 392, 395, 66 S.Ct. 582, 90 L.Ed. 743.

The three-year California statute of limitations (Code of Civil Procedure §338(4)) is applicable to the case at bar.[5]

Turner v. Lundquist (9th Cir. Apr. 7, 1967) 377 F. 2d 44 is squarely in point. It involved an action under provisions of the federal securities acts which appellants claim to be applicable herein. The court stated (before Hamley and Duniway, Circuit Judges, and Copple, District Judge):

> "This action was brought for monetary relief based on alleged violations of Section 10(b) of the Securities Exchange Act of 1934 (15 USC Sec. 78j(b)), Rule X-10B-5 of the Rules and Regulations of Securities Exchange Commission (17 CFR 240, 10B-51); and Section 17(a) of the Se-

[5]The parties, throughout the state and federal court proceedings, have considered only California as the state whose laws would be applicable.

curities Act of 1933 (15 USC Sec. 77q); plaintiff-appellant Turner likewise contends that he is entitled to damages for fraud and deceit under California state law."

. . . . . .

"Since there is no federal statute of limitations applicable to 15 USC §78b and 15 USC §77q, California's three-year statute [California Code of Civil Procedure, Section 338 (4)] is applicable. *Errion v. Connell* (9th Cir. 1956), 236 F. 2d 447. The lower court so found and counsel for both parties agree that this is the longest period applicable to each count in the complaint."

. . . . . .

"Federal procedure does not require a plaintiff to allege the time and circumstances of the discovery of the fraud in his complaint. However, when the matter is raised on defendant's motion for summary judgment the plaintiff cannot save his evidence until trial but 'must sufficiently disclose what the evidence will be to show that there is a genuine issue of fact to be tried.' *Matute v. Carson Long Institute, D.C.* 160 F. Supp. 827, 832, quoting from *Surkin v. Charteris* (5th Cir.) 197 F.2d 77, 79. See also *Kasey v. Molybdenum Corp. of Amer.* (9th Cir.), 336 F.2d 560, 575.

"In addition, the record reveals, and Turner has not denied, numerous facts which came to his attention prior to May 12, 1961 (three years prior to filing his amended complaint), sufficient in this view of the court to have put him upon notice and inquiry and commenced the running of the period of limitation as a matter of law. . . ." (377 F. 2d at pp. 45-48)

To the same effect:

Errion v. Connell (9th Cir. 1956) 236 F. 2d 447, 455;

Connelly v. Balkwill (DCND Ohio 1959) 174 F. Supp. 49 aff'd 279 F. 2d 865 (6th Cir. 1960);

Dack v. Shanman (SDNY 1964) 227 F. Supp. 26, 29.

See also:

Bromberg, *Securities Law: Fraud* (1967) Sec. 2.5(1) at p. 41.

It is apparent from the findings of fact in the first state court action (See Statement of the Case, supra p. 2, footnote (1) and R. 29)[6] that appellants, no later than December 30, 1961—*well over five years prior to filing their initial complaint in the court below*—knew or should have known of the existence of the facts which form the basis of their claim.

(b) Appellants' alleged claims accrued more than five years prior to filing.

Any causes of action appellants may have had against Beaman with respect to the contract of sale accrued not later than December 30, 1961. All pertinent facts were known to appellants by December 30, 1961. Unquestionably, the judgment in the first state court action was not entered until May of 1965 (Brief for Appellants p. 9) and $18,733.71 was not paid under such judgment until August of 1967 (Brief for Appel-

[6]See also Sackett's Supplemental Affidavit in Support of Preliminary Injunction (R. 46-48).

lants p. 7). However, these facts are immaterial to the question of the accrual of appellants' claims because:

(i) Appellants, by December 30, 1961, at the latest, could have commenced an action under the federal securities acts requesting return of the purchase price then paid ($1,000 and the promissory notes) and cancellation of the contract of sale.

Royal Air Properties, Inc. v. Smith (9th Cir. 1962) 312 F. 2d 210, 213; after removal, 333 F. 2d 568 (1964) [A defrauded buyer can sue to rescind.]

Matheson v. Armbrust (9th Cir. 1960) 284 F. 2d 670 [Judgment affirmed for purchaser in an action under Rule 10b-5 to cancel contract of sale and for damages.]

Errion v. Connell, supra, [Judgment for stockholder affirmed in an action for cancellation and damages under sections of 1934 Act and Rule 10b-5.]

(ii) Appellants could also have requested damages under an out-of-pocket rule, i.e., the difference between the value of that with which they departed (the down payment and their dollar liabilities under the contract of sale), and that which they received (the stock in News Publishing Co.).[7]

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[7]It is difficult to determine what measure of damages appellants are seeking to be applied in their proposed second amended complaint (R. 251). No allegations are set forth as to the value of what appellants received to form the basis of an out-of-pocket measure. The gist of such complaint to some degree suggests a rescission measure, plus the amounts of interest, fees and costs which the judgment in the first state court action awarded to Beaman. Appellants carefully ignore the $1,000 paid by them in 1961.

California Civil Code §3343 states:

> "One defrauded in the purchase, sale or exchange of property is entitled to recover the difference between the actual value of that with which the defrauded person parted and the actual value of that which he received, together with any additional damage arising from the particular transaction. . . ."

See

Janigan v. Taylor (1st Cir. 1965) 344 F. 2d 781, 786, cert. denied 382 U.S. 879;

Estate Counselling Service, Inc. v. Merrill Lynch, Pierce, Fenner & Smith, Inc. (10th Cir. 1962) 303 F. 2d 527, 533;

Graf v. Sumpter (1st Dist. 1962) 207 Cal. App. 2d 391, 393, 24 Cal. Rptr. 590.

> "In general, damages for fraud are to be assessed as of the date of the fraudulent transaction *(Hancock v. Williams,* 99 Cal. App. 2d 80, 82 [221 P. 2d 129] *That would be the date of the contract by which plaintiffs' right to the property and their obligation to pay therefor became fixed."* [Emphasis added]

See, also,

McCue v. Bruce Enterprises, Inc. (4th Dist. 1964) 228 Cal. App. 2d 21, 30, 39 Cal. Rptr. 125.

Appellants argue that under the language of 15 USC §77q a violation occurred in August, 1967, when Beaman obtained "money or property" ($18,733.71) by means of an *alleged* prohibited statement or omis-

sion to state. (Brief for Appellants, p. 7.) Appellants, of course, ignore the fact that Beaman, in 1961, had received both "money" ($1,000 down payment) and "property" (the promissory notes) by means of the same alleged prohibited statement or omission to state, albeit, without the formal aid of the California Superior Court.

Beaman simply obtained the $18,733.71 by judicial decree. It would be ludicrous to conclude (as appellants have argued) that the money paid under a valid state court judgment gives rise to a cause of action.[7a] The court, in *Key Broadcasting System Inc. v. Griffith* (1953) 119 NYS 2d 174, 175 (Brief for Appellants, p. 8) describes such a situation as "anomalous" but by no means suggests it as a legal possibility; moreover, the court was simply applying the well recognized rule that statutes of limitations in general do not run against defensive relief.

See

1 *Witkin, California Procedure* §95 at pp. 600-601.

It follows that appellants' claims against Beaman, whether founded on the federal securities acts or otherwise accrued not later than December 30, 1961, are time barred.

[7a]The court below stated:

"On that theory, every time the defendant in a lawsuit involving a personal injury loses it, he acquires damages as of the time the judgment is rendered . . . which, if improperly reached, creates a cause of action for damages." (Rep. Tr. p. 50.)

5. FINAL JUDGMENT IN THE FIRST STATE COURT ACTION CONSTITUTES A BAR BY REASON OF RES JUDICATA.

Since identity of parties and the entry of a final judgment in the state action are unquestionably present, the only element of res judicata which might legitimately be in doubt is that as to identity of issues.

See

McManus v. Bendlage (2nd Dist. 1947) 82 Cal. App. 2d 916, 922, 187 P. 2d 854 (discussing the three pertinent questions in determining the validity of a plea of res judicata).

The existence of an action based on the federal securities acts does not mean per se a different cause of action from an action in a state court based on the same facts. This is true even though 15 USC §78aa vests exclusive jurisdiction in the District Courts.

Connelly v. Balkwill (D.C.N.D. Ohio 1959) 174 F. Supp. 49, 56, aff'd 279 F. 2d 685 (6th Cir. 1960).

"Thus, while the courts of the several states have jurisdiction to determine actions based on fraud connected with the purchase or sale of securities, they have no jurisdiction in cases involving violations of Rule X 10b-5 which include the direct or indirect use of interstate facilities, the mails or the facilities of national security exchanges. It does not follow, however, that an action in Federal Court under Rule X 10b-5 is necessarily a different cause of action than an action in the state court based upon the same facts. The use of interstate facilities, the mails or the facilities of national security exchanges is not

per se a violation of Rule X 10b-5. Standing alone, the use of such facilities gives rise to no cause of action. The federal cause of action arises upon operative facts that disclose a violation of the provisions of the rule designed to insure fair dealing in connection with the sale and purchase of securities. While there has been no definitive determination of the boundaries of Rule X 10b-5, the better reasoned view is that—facts which would sustain a common law action for fraud might also constitute a cause of action under Rule X 10b-5 but not all cases arising under the rule would constitute a common law action for fraud. In *Beury v. Beury,* 127 F. Supp. 786, the District Court expressed the opinion that Section 10 of the Act conferred jurisdiction to entertain only those actions which involve a right of recovery which goes beyond common law rights. Although the appeal in that case was not from a final order and for that reason was dismissed, the Court of Appeals gratuitously expressed its disagreement with the above view of the trial judge. *Beury v. Beury,* 4 Cir. 22 F. 2d 464, at page 465. In Loss on Security Regulations, at 819, the author says: 'The extent to which the Security Exchange Acts go beyond common law fraud depends upon the particular common law jurisdiction.' Plaintiffs concur in this view and concede that in some jurisdictions the duty of disclosure under state law is no less strict than the duties imposed by Rule X 10b-5.

"To determine whether this case and the previous one are based upon the same cause of action, it is necessary first to ascertain the principles that govern actions of fraud in Ohio. . . ."

The District Court continued, after the foregoing quote, with an extensive discussion of fraud actions under Ohio law, concluding that the duty to disclose material facts under Ohio law is as broad and exacting as the duty of disclosure defined by Rule 10b-5.

Under California law, deceit may be negative as well as affirmative. It may consist of suppression of that which is one's duty to disclose as well as by declaration of that which is false, e.g., *Lingsch v. Savage* (1st Dist. 1963) 213 Cal. App. 2d 728, 735, 29 Cal. Rptr. 201.

The principle of disclosure is not confined to fiduciaries, having application to other relationships, e.g., vendor-vendee.

> *SanFran Co. v. Rees Blow Pipe Mfg. Co.* (1st Dist. 1959) 168 Cal. App. 2d 191, 207, 335 P. 2d 995.

Nor does the law of California countenance half truths.

> Calif. Civil Code §1710(3);
>
> *American Trust Co. v. California Western States Life Ins. Co.* (1940) 15 Cal. 2d 42, 65, 98 P. 2d 497.

Generally, the question is stated in 23 Cal. Jur. 2d 5, as follows:

> "Fraud in California is so broad and assumes so many shapes that courts are cautious in attempting to define it."

See also Calif. Corporations Code §3018.

It seems unnecessary to launch an extended discussion of the rules of fraud in California. In light of the foregoing considerations, California must be assigned a place among those " 'more enlightened jurisdictions' where the duty to disclose material facts is as broad and exacting as the duty of disclosure defined by Rule X 10b-5." (*Connelly v. Balkwill,* supra, 174 F. Supp. at p. 60, wherein Ohio was the subject of such quotation.)

The rule of res judicata is designed to prevent vexatious litigation and to require litigants to rest on one decision which includes not only matters actually determined by judgment, but also every other matter which the parties might have litigated as an incident thereto or essentially connected with the subject matter of the litigation, both in respect to matters of claim and of defense.

> *Panos v. Great Western Packing Co.* (1943) 21 Cal. 2d 636, 637-638;
>
> *Holman v. Holman* (4th Dist. 1938) 25 Cal. App. 2d 445, 452, 77 P. 2d 515.

See *Brunswig Drug Co. v. Springer* (2d Dist. 1942) 55 Cal. App. 2d 444, 449-50:

> "A party cannot by *negligence* or *design* withhold issues and litigate them in consecutive actions" (emphasis added).

Purported violations of the federal securities acts could have been raised by appellants as a defense to Beaman's complaint in the first state court action,

notwithstanding exclusive federal jurisdiction of actions under the 1934 Act and Rule 10b-5.[8]

Southern Brokerage Co. v. Cannosara (Tex. Civ. App. 1966) 405 SW 2d 457, error ref. NRE, cert. denied 386 U.S. 1004;

Key Broadcasting System, Inc. v. Griffith (1953) 119 NYS 2d 174 (cited in Brief for Appellants p. 8).

See *Red Rock Cola v. Red Rock Bottlers* (5th Cir. 1952) 195 F. 2d 406 (A state court has jurisdiction in suit on contract over a defense based on federal anti-trust laws.)

See, also, 1A *Moore's Federal Practice* (2d edition) ¶0.208[4] at p. 2325.

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6. APPELLANTS ARE BARRED BY THE DOCTRINE OF COLLATERAL ESTOPPEL.

In *Connelly v. Balkwill,* supra, the District Court determined that if res judicata were not a bar because more than one cause of action were involved, nevertheless, the plaintiffs therein were barred by the related doctrine of collateral estoppel (174 F. Supp. at pp. 60-61):

> "The doctrine of collateral estoppel, which is a narrowed version of res judicata, is based upon the principle that—

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[8]State courts have concurrent jurisdiction of claims under purported violations of 15 USC §77q. See 15 USC §77v.

'Where a fact essential to the judgment is actually litigated and determined by a valid and final judgment, the determination is conclusive between the parties in a subsequent action on a different cause of action.' (Restatement of Judgment §68, p. 293)

"The distinction between res judicata and collateral estoppel is delineated clearly in *United States v. International Building Co.,* 345 U.S. 502, at pages 504-505, 73 S.Ct. 807, 808, 97 L.Ed. 1182:

'The governing principle is stated in *Cromwell v. County of Sac.,* 94 U.S. 351-352-353, 24 L.Ed. 195. A judgment is an absolute bar to a subsequent action on the same claim.

'"But where the second action between the same parties is upon a different claim or demand, the judgment in the prior action operates as an estoppel only as to those matters in issue or points controverted, upon the determination of which the findings or verdict was rendered. In all cases, therefore, where it is sought to apply the estoppel of a judgment rendered upon one cause of action to matters arising in a suit upon a different cause of action, the inquiry must always be as to the point or question actually litigated and determined in the original action, not what might have been thus litigated and determined. Only upon such matters is the judgment conclusive in another action."'"

The court concluded that plaintiffs specifically were estopped by the state court judgments from again raising the issue of the materiality of certain nego-

tiations, since the state court had held that they were immaterial (174 F. Supp. at p. 62). Such argument has equal application to our facts if we assume (but not concede) that the action under the federal securities acts is a different cause of action from a fraud suit under California law.

Materiality and reliance are carried over from common law fraud actions to actions under the federal securities acts.

> *Janigan v. Taylor* (1965) 344 F. 2d 781, Cert. denied 382 U.S. 879;
> *List v. Fashion Park, Inc.* (1965) 340 F. 2d 457, Cert. denied 382 U.S. 811.

The findings in the first state court action clearly reflect that the subject contract was not executed under a material mistake and that such contract was not void for material mistake or for fraud (R. 29). In the words of Justice Molinari, who wrote the unanimous opinion affirming the judgment of the trial court in the first state court action (R. 229-230):

> "Accordingly, upon the basis of the evidence adduced, which was favorable to plaintiff, the trial court could reasonably conclude that the mistake contained in the profit and loss statement was neither a material mistake nor one that induced defendant to enter into the contract, but that defendant made his decision to purchase stock in News Publishing Company primarily upon the basis of his close relationship with de Menzes, as to whom defendant had great respect, his belief that Portsmouth was a promising area

> for a newspaper, and the favorable impression he received of the newspaper itself from examining back copies."[8a]

Thus, assuming (but not conceding) that a mistake, other act or omission might be material under the federal securities acts but not under California law relative to fraud, the finding in the first state court action that Sackett and KVAN did not rely on any mistake, other act or omission is sufficient to bar the instant action.

It is painfully clear that plaintiffs are simply attempting to relitigate issues which were carefully considered in the first state court action. More remarkable is the reference by appellants to an alleged $37,612.34 operating loss as of October 31, 1961, alleged to have been suffered by News Publishing Company (Brief for Appellants, p. 2). The record in the first state court action "is devoid of evidence showing the newspaper's financial position after August 24, 1961." (R. 234)

Sackett chose not to submit in the first state court action any evidence of the corporation's financial condition after August 24, 1961. It was the duty of Sackett and KVAN, at the trial in the first state court action, to tender each item of evidence tending to support their claims. Where they failed to do so, they are foreclosed from such action at trial of a subse-

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[8a]de Menzes was the major stockholder, president, general manager, director of News Publishing Company and a long time friend of Sackett (R. 229).

quent suit, and a claim that they have never had their day in court cannot be sustained.

Ernsting v. United Stages, Inc. (1929) 209 Cal. 733, 276 P. 103;

Bank of America v. McLaughlin (1937) 22 Cal. App. 2d 411, 71 P. 2d 291, 72 P. 2d 554;

Denio v. Huntington Beach (1946) 74 Cal. App. 2d 424, 431-32, 168 P. 2d 785.

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7. APPELLANTS ARE BARRED BY LACHES.

Apart from any consideration of a state statute of limitations, the doctrine of laches is applicable to bar appellants' claim.

Royal Air Properties, Inc. v. Smith (9th Cir. 1962) 312 F. 2d 210, 214;

Trussell v. United Underwriters, Limited (D.C. Colo. 1964) 228 F. Supp. 757, 776;

See: *Bromberg, Securities Law:* Fraud (1967) Sec. 11.5 at p. 253.

The findings of the court below (R. 264, line 20 to R. 265, line 10) supporting its conclusion of laches (R. 265, lines 24-27) have not been specified as error in appellants' brief.[9]

Rule 18(1)d, *Rules of the United States Court of Appeals for the Ninth Circuit.*

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[9]In fact, none of the findings of the court below have been specified as error in appellants' brief.

Consequently, such findings are not in issue and are not discussed herein.

Rule 18(3), *Rules of the United States Court of Appeals for the Ninth Circuit.*

In no measure were appellants "encased" (Brief for Appellants, p. 18) in a state court with respect to their rights under the federal securities acts *except by their own inaction.* Upon commencement of the first state court action by Beaman, appellants could have:

(i) defended, *inter alia,* on the grounds of alleged violation of the federal securities acts. (See discussion, supra, pp. 20-21)[9a]; or

(ii) commenced an action in the Federal District Court based on an alleged violation of the federal securities acts, requesting, alternatively, (a) rescission and return of moneys paid and property delivered, or (b) consequential damages. (See discussion, supra, p. 14.) To avoid piecemeal litigation, appellants at the same time could have requested the Federal District Court to exercise pendent jurisdiction over the non-federal issues in the first state court action.

Hurn v. Oursler (1933) 289 U.S. 238, 246, 53 S.Ct. 586;

See 1 *Moore's Federal Practice* ¶0.60[1] at p. 602.

[9a]The record in the second state court action will show that appellants did plead violations of the federal securities acts as defensive matter (answer and cross-complaint of Sackett and KVAN, p. 6, line 29 to p. 7, line 22). While few of the documents

In non-constitutional cases and in the absence of special circumstances, a federal court having jurisdiction should normally proceed to an adjudication of both state and federal issues.

County of Alleghany v. Frank Mashuda Co. (1959) 360 U.S. 185, 79 S.Ct. 1060, reh. denied 361 U.S. 855;

Propper v. Clark (1949) 337 U.S. 472, 489, 490-491, 492, 69 S.Ct. 1333;

See *Ballantine Brooks, Inc. v. Capital Distributing Co.* (2d Cir. 1962) 302 F. 2d 17, 19 (A federal court is not required to abate the normal *in personam* action on a plea of a pending action in a state court.)

See, also, 1A *Moore's Federal Practice* ¶0.203 [2] at p. 2123.

Thus, appellants were in no wise prevented from litigating the federal questions in a federal court upon discovery in 1961 of the facts giving rise to a purported claim under the federal securities acts.

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8. REPLY TO MISCELLANEOUS POINTS RAISED BY APPELLANTS.

(a) Appellants' Statement of the Case.

None of the alleged factual matters set forth in appellants' Statement of the Case (Brief for Appellants, pp. 2-4) is supported by reference to the record, ex-

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in such action are a part of the record on appeal herein, their existence and contents may be judicially noticed. *Shapleigh v. Mier* (1937) 299 U.S. 474, 81 L. Ed. 355, 359.

cept for two items under the heading "The Federal Suit" (Ibid. p. 4).[10]

Rule 18(2)C, *Rules of the United States Court of Appeals for the Ninth Circuit.*

Appellants' sketchy "Factual Background" (Brief for Appellants) attempts to create an impression that Sackett did not get what he fairly and openly bargained for. The findings of the first state court action negate any such impression (R. 28-29).

In reference to the findings in the first state court action, appellants speak of the "*now*[11] conceded falsity of" a financial statement as though any such concession occurred after judgment in such action. Clearly the fact (a calculation error) was before the trial court in such action (R. 227). Clearly the California appellate court felt there was substantial evidence to support the findings favorable to Beaman (R. 233).

The statement of appellants (their brief p. 4) that the judgment in the first state court action was satisfied is not correct (see Brief for Appellants p. 3 for a contrary statement).

(b) The Contention as to a Suspension of the Statute of Limitations.

Appellants argue that because of the California election of remedies doctrine, they were prevented

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[10]Appellants refer to an assignment to Fidelity and Deposit Company of Maryland for security purposes. (Brief for Appellants, p. 3) Such a fact (its accuracy is unknown to us) is outside of the record and immaterial to a determination of this appeal.

[11]Our emphasis.

from suing for damages in the federal court and thus the running of any statute of limitations is suspended (Brief for Appellants, pp. 11-12).

Appellants' authorities (Brief for Appellants, p. 12) support a rule of reason which would suspend an applicable statute of limitations whenever there was a *prevention* of a trial on the merits.

See, 1 *Witkin California Procedure* § 165, at pp. 674-675.

It should be noted first that the choice of remedies in the state court which appellants contend would block their claim for damages in the federal court was their own—not Beaman's. Clearly, there is a common sense qualification to any rule suspending a statute of limitations which would exclude a prevention *resulting from the act or omission of the party claiming a suspension.* None of appellants' authorities suggests that a suspension would be appropriate under the circumstances of this case.

In any event, appellants' statement of California law as to election of remedies and its application herein is incorrect. California Civil Code § 1692 provides:

> "When a contract has been rescinded in whole or in part, any party to the contract may seek relief based upon such rescission by (a) bringing an action to recover any money or thing owing to him by any other party to the contract as a consequence of such rescission or for any other relief to which he may be entitled under the circumstances, or (b) asserting such rescission by way of defense, counter-claim or cross-complaint.

"If in an action or proceeding a party seeks relief based upon rescission and the court determines that the contract has not been rescinded, the court may grant any party to the action any other relief to which he may be entitled under the circumstances.

"*A claim for damages is not inconsistent with a claim for relief based upon rescission. The aggrieved party shall be awarded complete relief, including restitution of benefits, if any, conferred by him as a result of the transaction and any consequential damages to which he is entitled; but such relief shall not include duplicate or inconsistent items of recovery.*

"If in an action or proceeding a party seeks relief based upon rescission, the court may require the party to whom such relief is granted to make any compensation to the other which justice may require and may otherwise in its judgment adjust the equities between the parties." (Emphasis added)

The purpose of such statute is obviously to prevent duplicate or inconsistent relief. Since appellants could have added a cause of action for damages in the first state court action, a fortiori, they could have filed such an action in the federal courts without being met with a contention that their claim for rescission had been abandoned.

Williams v. Marshall (1951) 37 Cal. 2d 445, 457, 235 P. 2d 372.

Nothing prevented a trial on the merits in the federal court. (See discussion, supra, at p. 26.)

(c) The Contention That a Federal Court Is Not Bound to Apply the State Statute of Limitations.

Appellants assert that federal courts are not bound to apply a state statute of limitations where "in a proper case it would defeat the assertion of federal rights," citing *Fischbach & Moore, Inc. v. Int'l Union* (SD Calif. 1961) 198 F. Supp. 911 (Brief for Appellants, p. 13).

Fischbach & Moore, supra, involved an action for damages arising out of unfair labor practices by labor unions. The alleged activities occurred more than three, but less than five, years before the action was filed. The court reached its decision to ignore any state limitations on the basis of the *Lincoln Mills* case, 353 U.S. 447, 77 S.Ct. 912, which clearly expressed a policy as to the Labor Management Act, i.e., that federal courts were bound to apply not state substantive law, but federal substantive law to be fashioned from the policy of national labor laws (198 F. Supp., at p. 913).

Appellants' assertion simply ignores the several federal court decisions which have determined that state statutes of limitations are to be applied in actions under the federal securities acts where no federal provision has been made therefor.

> *Turner v. Lundquist,* supra, and other cases cited in the discussion, supra, p. 11.

In any event, the court stated in *Fischbach & Moore, Inc.,* supra (198 F. Supp., at p. 915):

> ". . . as a practical matter the equitable doctrine of laches may be utilized to preclude re-

covery in any case where it appears that the plaintiff has delayed unnecessarily in asserting his claim. . . ."

(d) Application of England v. Louisiana Medical Examiners.

Appellants rely exclusively on *England v. Louisiana State Bd. of Medical Examiners* (1964) 375 U.S. 411, 84 S.Ct. 461 as authority for their contention that there was error in holding appellants' claims were barred by res judicata and collateral estoppel (Brief for Appellants, pp. 15-20).

The plaintiffs in *England* were graduates of chiropractic schools seeking to practice in Louisiana without complying with a Louisiana state statute. Action was commenced in the local federal district court seeking an injunction and a declaration that the state statute as it applied to them was unconstitutional. That court invoked the abstention doctrine and entered an order staying further proceedings therein until Louisiana courts had an opportunity to determine certain issues, with an express reservation of jurisdiction; and plaintiffs then brought an action in the Louisiana courts to determine whether the state statute applied to them. It was in the latter proceeding that plaintiffs argued the federal constitutional question, and lost.

Next, plaintiffs returned to the Federal District Court for a determination of their constitutional claim. The United States Supreme Court held that the state court proceedings were not a bar to the constitutional question.

The facts in *England,* supra, are far different from ours:

1. Appellants did not go to the federal court in the first instance. Thus, they did not invoke federal jurisdiction and become compelled to go to the state court by order of the federal court.

2. No questions of constitutionality are involved. Thus, there would have been no necessity for application of the doctrine of abstention. (See discussion, supra, p. 27.)

3. Appellants were free to commence an action in the Federal District Court on the federal claims. Thus, they were not free from fault in accepting a state court's determination of their claims. (See discussion, supra, at p. 26.)

Furthermore, it is clear under the federal removal statutes (28 USC §§ 1441-1450) and discussions interpreting them, that in absence of a fraudulent purpose to defeat removal, a plaintiff may, by the allegations of his complaint, determine the status with respect to the removability of a case. This power to determine removability continues with the plaintiff throughout the litigation. Thus, the avowed helplessness of appellants to remove (Brief for Appellants, p. 19) is nothing new or different; nor is it a cause of sustaining their contentions.

Great Northern Railway Co. v. Alexander (Hall's Adm'n) (1918) 246 U.S. 276, 282, 62 L.Ed. 713;

1A *Moore's Federal Practice,* ¶0.160 at p. 473.

CONCLUSION

Any deprivation of a chance to *assert* a federal remedy which appellants have suffered has been effected by appellants through their own acts or omissions.

Wherefore, Beaman respectfully submits that the judgment of the court below should be affirmed.

Dated, San Francisco, California,
February 15, 1968.

Respectfully submitted,
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J. Frank Beaman.

I certify that in connection with the preparation of this brief I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit and, in my opinion, the foregoing brief is in full compliance with these rules.

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